



House Bill 1050: Omnibus Tax Law Changes.

2013-2014 General Assembly

Committee:	House Finance	Date:	May 14, 2014
Introduced by:	Representatives Howard, Bill Brawley, Lewis, and Setzer	Prepared by:	Cindy Avrette Committee Counsel
Analysis of:	House Bill 1050		

SUMMARY: *House Bill 1050 makes various tax law changes recommended by the Revenue Laws Study Committee. The Revenue Laws Study Committee met each month during the interim and began reviewing bill drafts at its November meeting. The Committee posted the drafts on its website; received comments from taxpayers, the Department of Revenue, and other interested parties; and held committee discussions. The Committee's meeting materials may be found on its website. [Revenue Laws Committee Documents](#)*

PART I DEDUCTION FOR STATE NET LOSS

SUMMARY: *Part I of the Omnibus Tax Law Changes bill would replace the corporate net economic loss deduction with a State net loss deduction for taxable years beginning on or after January 1, 2015.*

CURRENT LAW: Both federal and State tax law provide relief to a corporation that incurs more expenses than revenues during the taxable period. For federal tax purposes, a corporation is allowed a net operating loss deduction equal to the amount by which tax deductible expenses are more than taxable revenues. The federal deduction may be carried back two years preceding the loss year, thus providing immediate tax relief in the form of a tax credit; any unused portion of the deduction may be carried forward for 20 years. For State tax purposes, a corporation is allowed a net economic loss deduction¹ equal to the amount by which allowable deductions for the year other than prior year losses exceed income from all sources in the year, including nontaxable income.² The State deduction may be carried forward 15 years; any loss carryforward must first be offset by nontaxable income, including allowable deductions.

BILL ANALYSIS: This Part does three things to simplify the calculation and ease the administration of the corporate loss deduction, effective for taxable years beginning on or after January 1, 2015:

¹ NC is the only state with a net economic loss deduction that differs significantly from the federal net operating loss deduction. Other states that have a corporate income tax loss deduction use a calculation that is comparable to the federal net operating loss deduction.

² Nontaxable income includes income that has been deducted in computing State net income, nonapportionable income that has been allocated directly to another state under G.S. 105-130.4, and any other income that is not taxable under State law. Prior to August 17, 2013, the Department of Revenue interpreted G.S. 105-130.8 to require items deductible under G.S. 105-130.5, such as U.S. government interest and dividends, to be considered in the computation of the loss in the year of creation as nontaxable income. The Department revised its interpretation to recognize that an allowable deduction, although not taxable, may not reduce a loss in the year the loss is created. However, pursuant to G.S. 105-130.8(a)(3), the Department continued to require that a loss carried forward to a subsequent year must first be offset by any income not taxable, including allowable deductions under G.S. 105-130.5.



- It replaces the net economic loss calculation with a State net loss calculation that is more comparable to the federal net operating loss calculation.
- It removes the requirement that a net economic loss carried forward to taxable years beginning on or after January 1, 2015, be first offset by nontaxable income.
- It instructs the Secretary of Revenue to apply the standards under sections 381 and 382 of the Code when determining to what extent a loss survives a merger or an acquisition.

The Part would replace the State's net economic loss deduction with a State net loss deduction. The State net loss would be the amount by which allowable deductions for the year, other than prior year losses, exceed gross income under the Code for the year adjusted as provided in G.S. 105-130.5. Adjustments under G.S. 105-130.5 include items such as the adjustments taxpayers must make when the State decouples from federal accelerated depreciation and expensing. If the taxpayer is a multi-state corporation with business within and without North Carolina, then the loss must be allocated and apportioned in the year of the loss in accordance with G.S. 105-130.4.

The repeal of the net economic loss deduction removes the applicability of North Carolina case law that governs the extent to which a net economic loss survives in a merger or an acquisition. The draft instructs the Secretary of Revenue to apply the federal regulations adopted under sections 381 and 382 of the Code in determining the extent to which a loss survives in a merger or acquisition. Although the provisions of the Code would be applied, the loss limitations may differ at the State level based upon the single entity reporting requirement in North Carolina and subject to the allocation and apportionment provisions of G.S. 105-130.4 in the year of the loss.

The Part changes the calculation of a net economic loss carry-forward. Under current law, the carry-forward must be reduced by nontaxable income. What constitutes nontaxable income has been a source of questions, disagreements, and litigation. Under the change made by this Part, the amount of the net economic loss, as determined on December 31, 2014, becomes a static amount. Any unused portion of a net economic loss carried forward in taxable years beginning on or after January 1, 2015, would be administered in accordance with the State net loss statute:

- Any unused portion of a net economic loss would not have to first be offset by nontaxable income.
- The standards under sections 381 and 382 of the Code would be applied in determining the extent to which a net economic loss survives a merger or acquisition that occurs on or after January 1, 2015.

EFFECTIVE DATE: This Part would become effective for taxable years beginning on or after January 1, 2015.

PART II. OTHER INCOME TAX CHANGES

SUMMARY: *Part II of the Omnibus Tax Law Changes bill makes technical and clarifying changes to various income tax laws.*

CURRENT LAW, BILL ANALYSIS, AND EFFECTIVE DATE: This Part makes the following technical and clarifying changes to the income tax laws.

Section 179 expense deduction

Section 2.1 makes two changes to the section 179 expense deduction for State income tax purposes to reflect the intent of legislative action taken in 2013. These changes need to be enacted as soon as possible since the changes impact 2013 tax returns. Many taxpayers have filed extensions, waiting for these provisions to be enacted.

First, it corrects the dollar amount of the section 179 expense investment limit. In the American Taxpayer Relief Act of 2013, Congress extended the \$500,000/\$2,000,000 accelerated section 179 expense deduction allowances for 2013 and 2014. The intent of S.L. 2013-10 was to decouple from this federal provision and return to the limits that would have been applicable under the Code as written in December 2010. The act erroneously referred to the Code as defined in May 2010. The Code was amended three times in 2010, and the changes included three different section 179 expense limits. S.L. 2013-414 rewrote the statutes that decouple from the federal accelerated depreciation expensing to make them clearer to understand. As part of the rewrite, the subsection decoupling from the section 179 expense limits sets forth the limits as opposed to referring to the Code on a certain date. In setting forth the limits, the dollar amount of the investment limit should have been \$200,000 rather than \$125,000.

Second, it makes changes to ensure that qualifying taxpayers may receive the benefit of the add-back deductions. Beginning in 2002, Congress has allowed taxpayers to depreciate certain assets more quickly than would otherwise be allowed – 100% bonus depreciation and section 179 expense deductions. Many states, including North Carolina, have decoupled from those provisions primarily because the fiscal impact of conforming to the greater depreciation rules would have been too costly. Instead of granting the larger depreciation in the initial years, North Carolina required taxpayers to add-back 85% of the deduction in the first year and to deduct 20% of this amount over the next five years. Taxpayers who changed their form of business entity or who merged with subsidiaries within the five-year period of deductions were not allowed to take the remaining deductions because the taxable entity that made the add-back and received the initial deductions either no longer existed or no longer owned the depreciable asset. The result in some cases was that the asset did not receive the full benefit of the deduction. S.L. 2013-414 changed the law to allow the transferee of an asset, where the tax basis of the transferred asset carried over from the transferor to the transferee for federal income tax purposes, to add any remaining deductions to the basis of the transferred asset and to depreciate the adjusted basis over the remaining life of the asset. For transactions that occurred prior to January 1, 2013, the law provided an election whereby the transferee could make the basis adjustment for any deductions foregone by the transferor. However, this allowance does not help a taxpayer who had disposed of the asset or whose asset had no remaining useful life. This section remedies this situation by allowing a taxpayer to deduct the remaining bonus depreciation on the 2013 tax return.

Personal income tax deductions

Section 2.2 does the following two things.

First, it clarifies that a person who is not eligible for a federal standard deduction is not eligible for a State standard deduction. North Carolina follows the federal law concerning an individual's eligibility for a standard deduction. The tax reform legislation inadvertently failed to follow this practice. Under federal law, the following individuals are not eligible for a standard deduction:

- A married individual filing a separate return where either spouse itemizes deductions.
- A nonresident alien individual. A resident alien is a person who meets either the “green card test” or the “substantial presence test”.
- An individual making a return for a period of less than 12 months on account of a change in the person's annual accounting period.

- An estate or trust, common trust fund, or partnership.

Second, it clarifies the application of the \$20,000 deduction for mortgage interest expenses paid and property taxes paid on real estate. S.L. 2013-316 limited the federally allowed itemized deductions for mortgage interest expenses paid and property taxes paid on real estate at \$20,000. The intent of the legislation was for the \$20,000 cap to apply to the cumulative deduction for a married couple, regardless of how the couple files a return. At the request of the Department of Revenue, this section clarifies this intent.

This section would become effective for taxable years beginning on or after January 1, 2014.

Income tax rate applicable to estates

Section 2.3 updates the statutory references in G.S. 105 160.2 which imposes income tax on estates and trusts. Estates and trusts generally receive the same modifications to taxable income and tax rates as single individuals. House Bill 998, S.L. 2013 316, moved the statutes allowing modifications to North Carolina taxable income and setting the tax rate.

This section would become effective for taxable years beginning on or after January 1, 2014.

PART III. AGRICULTURAL EXEMPTION CERTIFICATE

SUMMARY: Part III of the Omnibus Tax Law Changes bill gives guidance to the farming community and the Department of Revenue as to the administration of the income threshold a person must meet to qualify for a sales tax agricultural exemption certificate. It also allows a three-year income averaging to address issues of income volatility in farming operations.

CURRENT LAW: In S.L. 2013-316, the General Assembly imposed an income threshold a person must meet to qualify for a sales tax agricultural exemption certificate. Effective July 1, 2014, a person does not qualify for an agricultural exemption certificate unless the person has an annual gross income for the preceding taxable year³ of at least \$10,000 from farming operations. For federal income tax purposes, gross income from farming includes sales of agricultural products, cooperative distributions, agricultural program payments, and crop insurance and federal disaster payments. It appears five other states impose an income requirement to qualify for a sales tax agricultural exemption: Connecticut, Georgia, Rhode Island, Tennessee, and Washington. The income limit in these states varies from \$1,000 in Tennessee to \$10,000 in Washington. Four of those states have conditional exemption certificates for new farmers.

An agricultural exemption certificate allows a person to purchase the following items for farming operations without paying sales tax on those items: fuel; electricity; commercial fertilizer, lime, land plaster, plastic mulch, plant bed covers, potting soil, baler twine, and seeds; farm machinery; attachments and repair parts for farm machinery; containers used in farm production, packaging, and transporting; grain, feed, or soybean storage facilities; substances for use on animals and plants, such as vaccines, insecticides, defoliants, and plant growth regulators; baby chicks; facilities used for housing, raising, or feeding animals; and bulk tobacco barns and parts and accessories for those barns.

A person who qualifies for an exemption certificate must apply to the Department. A certificate is valid until it is cancelled or revoked. An exemption certificate authorizes the retailer to sell an item to the

³ The statute currently says "calendar year". The Department has requested that the term be changed to "taxable year". The bill draft makes this change.

holder and either collect tax at a preferential rate or not collect tax on the sale, as appropriate. A retailer does not need to obtain a certificate for each purchase if the retailer has a blanket certificate from a purchaser with which the retailer has a recurring business relationship. A person who purchases an item with a certificate is liable for any tax due on the sale if the Department determines the person is not eligible for the certificate. The statute does not place an affirmative duty on the holder of a certificate to notify the Department if the person no longer qualifies for it.

BILL ANALYSIS: Part III of the bill answers questions the farming community has posed concerning the implementation of the gross income requirements:

- **Administration.** – The bill clearly states that a person may not use an agricultural exemption certificate after July 1, 2014, unless the person meets the income requirements and that a person who no longer qualifies for the certificate is liable for any tax due. A qualifying farmer must apply to the Department for a new exemption certificate. A retailer may continue to rely upon a blanket certificate until October 1, 2014.
- **Application for Certificate.** – Neither the law enacted last year nor this bill changes the current administration of exemption certificates. However, the bill does impose an affirmative duty on a person who has an exemption certificate to notify the Department whenever the person no longer qualifies for it and to give notice to any seller that may rely on it. The affirmative duty applies to all holders of a certificate, not just farmers. This affirmative duty is similar to the one imposed on taxpayers who no longer qualify for preferential property tax treatment. The farming community is familiar with this requirement as part of the present use value property tax exemption program.
- **Liability for Tax Due.** – The bill affirmatively states that anyone who purchases an item under an exemption certificate is liable for the tax due on the purchase if the Department determines that the person is not eligible for the certificate or that the item purchased does not qualify for exemption under the certificate.
- **Income Volatility.** – The bill makes a substantive change to the income threshold at the request of the farming community to address volatility in farming income and to prevent a person from moving into and out of the exemption annually. To obtain a certificate, a person must have \$10,000 of gross income from farming operations during the preceding taxable year or an average of \$10,000 of gross income from farming operations for the three preceding taxable years. A farmer no longer qualifies for the exemption certificate when the farmer fails to meet the income threshold for three consecutive years. The Farm Bureau expressed concerns for certain types of farming operations that may not produce income on an annual basis, such as cattle breeders and timber operations.

EFFECTIVE DATE: This Part of the bill would become effective July 1, 2014, and applies to purchases made on or after that date.

BACKGROUND: There are currently 49,437 agricultural exemption certificates outstanding. Last year the Department issued 2,185 new certificates and it issued 2,253 certificates in 2012. Here are some statistics from the 2012 USDA Census of Agriculture:

	2012	2007
Total NC Farms	50,218	52,913
NC Farms < \$10,000 in sales	31,492	34,276
NC Farms > \$10,000 in sales	18,726	18,637
NC Farms < \$10,000 in sales & government payments	30,960	33,741
NC Farms > \$10,000 in sales & government payments	19,258	19,172

PART IV. PREPAID MEAL PLANS

SUMMARY: *Part IV of the Omnibus Tax Law Changes bill addresses sales tax issues related to the repeal of the sales tax exemption for meals served to students in dining rooms of regularly operated educational institutions.*

CURRENT LAW: S.L. 2013-316 repealed the exemption for meals served to students in dining rooms of regularly operated by educational institutions, effective January 1, 2014. In practice, meals are not always sold directly. Today, educational institutions sell a variety of meal plans that offer choices between a specific number of "meal swipes" and "food dollars". The meal swipes are part of a prepaid meal plan that entitles the student to a predetermined number of meals. The cost applies regardless of whether or not the student consumes the meals. The food dollars are part of a declining card balance, much like a debit card, that may be used in on-campus facilities for a variety of purchases as well as with participating privately-owned facilities. The meal swipes are problematic to tax on a transactional basis because the gross receipts paid for the meal swipes applies regardless of whether or not the meals are consumed. In practice, few institutions operate their dining halls; instead, they contract with third party vendors to prepare the meals and operate the dining halls.

BILL ANALYSIS: Part IV of the bill addresses questions and administrative issues taxpayers and the Department of Revenue have encountered with the taxation of food and prepared food sold to students in colleges and universities.

Subsection	Explanation
(a)	Defines a prepaid meal plan to be a plan offered by an institution of higher education that entitled a person to food or prepared food, that is billed or paid for in advance, and that provides for predetermined units or unlimited access to food or prepared food but does not include a dollar value that declines with use. The definition limits the applicability to those transactions that benefited from the sales tax exemption repealed in S.L. 2013-316. It does not apply to the part of a meal plan that is based on a declining card balance, such as the food dollars, because those transactions are taxed at the time they are made. By

	applying the tax to the gross receipts derived from the plan, it is clear that that the tax is based upon the amount paid for the plan and not upon the use of the plan.
(b)	Imposes a sales tax at the general rate upon the sales price of or gross receipts derived from a prepaid paid meal plan. The local sales tax also applies to an item taxed by the State at the general sales tax rate.
(c)	Sources the local sales tax revenue to the county where the school is located.
(d)	Addresses how to tax a transaction where one amount is paid for a taxable item (prepaid meal plan; meals) and a nontaxable item (declining card balance; tuition; room). In that instance, tax applies to the allocated price of the prepaid meal plan. The tax applies to items purchased with a dollar value that declines with use as the dollar value is used. Tuition and room are not subject to sales tax.
(e)	<p>This subsection does two different things:</p> <p>Clarifies that the remaining sales tax exemption for meals sold in elementary and secondary schools applies to any school regulated under Chapter 115C. Public K-12 schools, private K-12 schools, regional schools, and home schools are regulated under Chapter 115C. Residential schools are regulated elsewhere.⁴ The bill removes the words "not for profit" because meals provided to K-12 students take many forms. This change ensures that the tax treatment for meals sold in elementary and secondary schools remains unchanged until the General Assembly makes a policy choice to tax them differently.</p> <p>Exempts food and prepared food used to prepare a meal for consumption under a prepaid meal plan from sales tax because this transaction is analogous to a sale for resale.</p>
(f)	Provides schools with an option for reporting and remitting sale tax revenue derived from a prepaid meal plan to the State. The option allows the institution to contract with the food service contractor to be liable for the collection and remittance of the tax. At least one university has a contract with its food service contractor to remit the tax to the State on behalf of the university. The university remains the retailer under the sales tax laws because it is the person making, offering, and soliciting the sale of the prepaid meal plan. The tax will apply to the gross receipts the university derives from the prepaid meal plan; this amount includes the amount charged the university by the food service contractor and any other expenses included by the university in the price it charges for the prepaid meal plan. Under this option, the retailer (institution) would send the tax receipts collected to the food service contractor and the food service contractor would send the receipts, along with other tax receipts, to the Department of Revenue.

EFFECTIVE DATE: This Part of the act would become effective when it becomes law and applies to gross receipts derived on or after that date. Colleges and universities will begin billing for the fall semester in July, and payments will be received primarily during the months of July and August.

⁴ The School of Math and Science and the School of the Arts are part of the UNC system.

PART V. ADMISSIONS

SUMMARY: *Part V of the Omnibus Tax Changes bill draft addresses sales tax issues associated with the expansion of the sales tax base to include gross receipts derived from admissions to a live event, a movie, and other attractions for which an admission is charged.*

CURRENT LAW: S.L. 2013-316 changed the taxation of live events and movies from a 3% gross receipts privilege tax to a State and local sales tax. The two taxes differ in that the gross receipts tax was imposed upon the person engaged in providing the event; it was not designed to be passed directly onto the consumer. The sales tax is imposed upon the retailer, but it is intended to be passed onto the purchaser and borne by the purchaser instead of the retailer.⁵ The payment of the tax is considered a debt from the purchaser to the retailer until it is paid. A retailer is considered to act as a trustee on behalf of the State when it collects tax from the purchaser. The tax should be stated and charged separately unless the retailer displays a statement indicating the sales price includes the tax.

The gross receipts tax was payable monthly and the return covered the gross receipts received during the previous month.⁶ The sales tax is due quarterly, monthly, or bi-monthly depending upon the tax liability of the retailer.⁷ The administration of the sales tax is more defined to ensure uniform tax treatment. North Carolina is also a member state in the Streamlined Sales Tax Agreement. One of the purposes of this Agreement is to ensure uniformity among the participating states so the tax may be more efficiently administered by retailers who conduct business in more than one state.

BILL ANALYSIS: This Part makes the following changes to the laws applicable to sales tax on the gross receipts derived from an admission charge:

Subsection	Explanation
(a)	Clarifies that for purposes of the imposition of sales tax, the term "gross receipts" has the same meaning as the term "sales price". "Sales price" is defined to be the total amount or consideration for which tangible personal property, digital property, or services are sold, leased, or rented. This subsection also removes the details concerning how amusements are taxed and moves those provisions to a new statute in subsection (c) of this section. The imposition of the tax itself remains in G.S. 105-164.4.
(b)	Sources the local sales tax revenue derived from admission charges to the location where admission to the entertainment activity may be gained. When the location where admission may be gained is not known at the time of the transaction, the general sourcing principles of G.S. 105-164.4B(a) apply: the business location where the product is received; the location where the product is received; the location indicated by the address of the purchaser.
(c)	Creates a new statute to address the taxation of admission charges: <ul style="list-style-type: none"> It defines an "admission charge" as the gross receipts derived for the right to attend an entertainment activity. An entertainment activity is defined as a live performance, a movie, a museum or similar attraction and a guided tour of that attraction. The bill does not expand the definition the types of entertainment subject to the tax. The policy decision of what types of entertainment to include in the sales tax base was made in S.L. 2013-316. It defines an "amenity" as a feature that increase the value of an entertainment activity by giving the person access to items that are not subject to sales

⁵ G.S. 105-164.7.

⁶ By practice, some taxpayers remitted the gross receipts tax at the time the event occurred.

⁷ G.S. 105-164.16.

	<p>tax and that are not available with purchase of admission to the event without the feature. Lastly, it defines a facilitator. The law enacted last session did not define "admission charge" or "amenity". A definition of "facilitator" is needed to accomplish the administration of the tax as provided in this subsection.</p> <ul style="list-style-type: none"> • It provides that a retailer is the operator of the venue where the entertainment activity occurs. In practice, admission to an entertainment event may often be obtained at multiple places from multiple people. To accommodate this business practice, the bill does the following: <ul style="list-style-type: none"> ○ Provides that a person who provides the entertainment and received admission charges directly from purchaser is a retailer. This provision would allow a person, such as the symphony, that leases space to perform to be a retailer. In this example, the venue would also be a retailer if the venue also sells admission to the symphony event. ○ Provides the operator of the venue and a facilitator may have a contractual agreement for dual reporting. Dual remittance will allow the operator of the venue to remit the tax on the admission charge and the facilitator to remit the tax on any other charges the facilitator imposed that were necessary for the purchaser to pay to complete the transaction. • It defines a facilitator as a person who accepts payment of an admission charge to an entertainment activity and is not the operator of the venue where the entertainment activity occurs. It requires the facilitator to report to the retailer the admission charge a person pays to the facilitator and to send to the operator the tax due on the gross receipts derived from an admission charge no later than 10 days after the end of each calendar month. A facilitator that does not send this amount to the retailer is liable for the tax due. These requirements are considered terms of the contract between the retailer and the facilitator. These provisions are the same as the provisions applicable to facilitators who accept payment from a consumer for accommodations. • It clarifies what transactions are not subject to the tax: <ul style="list-style-type: none"> ○ Amounts paid to participate in sporting events. ○ Tuition, registration, or any other charge to attend an instructional or educational seminar, workshop, or conference. ○ A political contribution. ○ A charge for lifetime seat rights, leases, or rental of a suite or box, provided the charge is separately stated. ○ An amount paid solely for transportation. • It clarifies the following exemptions from the tax: <ul style="list-style-type: none"> ○ The portion of a membership charge that is deductible as a charitable contribution under federal income tax laws. ○ A donation that is deductible as a charitable contribution under federal income tax laws. ○ Charges for an amenity.
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	<ul style="list-style-type: none"> • It changes the events that are exempt from the tax to the following: <ul style="list-style-type: none"> ○ An event sponsored by an elementary or secondary school. ○ An event sponsored by a nonprofit that is exempt from income tax if all of the following conditions are met: the entire proceeds of the event are used exclusively for the entity's nonprofit purpose; the entity does not compensate members or individuals; the entity does not compensate any person for participating in the event, performing in the event, placing in the event, or producing the event. • It repeals the following exemptions, thus subjecting the gross receipts derived from an admission charge to that event to sales tax, effective January 1, 2015: <ul style="list-style-type: none"> ○ An agricultural fair. ○ Up to two activities a year sponsored by a nonprofit.⁸ ○ A State attraction.
(d)	Makes a conforming change to the exemption statute. This subsection becomes effective January 1, 2015.
(e)	Clarifies that long-standing exemptions applicable to tangible personal property sold by nonprofit entities do not apply to gross receipts derived from an admission charge to an entertainment activity.
(f)	Provides that the gross receipts derived from admission to a live event purchased on or after January 1, 2015, will be taxable under the sales tax statutes, regardless of the date of the initial sale of tickets. S.L. 2013-315 provided a transitional period. Under S.L. 2013-316, the gross receipts for a live event where the initial sale of admission occurred on or before January 1, 2014, are taxable under the old 3% gross receipts privilege tax statutes.

EFFECTIVE DATE: Except as otherwise provided, this Part of the act would become effective January 1, 2015.

PART VI. SERVICE CONTRACTS

SUMMARY: *Part VI of the Omnibus Tax Law Changes bill addresses sales tax issues associated with the expansion of the sales tax base to include the sales price of a service contract.*

CURRENT LAW: S.L. 2013-316 expanded the sales tax base to include the sales price of a service contract. A service contract is defined as a warranty agreement, a maintenance agreement, a repair contract, or a similar agreement or contract by which the seller agrees to maintain or repair tangible personal property. The act exempted from the tax items exempt from sales tax, other than motor vehicles; network assets on utility owned lands and on right-of-ways or easements; and items purchased by a professional motorsports racing team for which the team may receive a sales tax refund. The act

⁸ A subcommittee of the Revenue Laws Study Committee recommended that similar events be taxed similarly, regardless of the entity providing the event. This policy decision led to the repeal of these exemptions. The subcommittee also found that the exemptions caused confusion re: what was a State attraction and what two events could be exempt. This confusion should be eliminated by the repeal of these exemptions.

also exempted an item used to maintain or repair tangible personal property pursuant to a service contract if the purchaser of the contract is not charged for the item.

BILL ANALYSIS: This Part makes the following changes to the law applicable to the sales tax on service contracts:

Subsection	Explanation
(a)	Changes the definition of a service contract to alleviate confusion about who must provide the work under the service contract for the contract to be taxable. In practice, service contracts are often sold by a seller on behalf of the person obligated to provide the service. This subsection changes the definition of a service contract to be a contract where the obligor under the contract agrees to maintain or repair tangible personal property or a motor vehicle.
(b)	Clarifies in the sales tax imposition statute that the tax applies to the sales price of or the gross receipts derived from a service contract.
(c)	<p>Creates a new statute to address the sales tax on service contracts:</p> <ul style="list-style-type: none">• It clarifies that the local sales tax revenue from a service contract are sourced in accordance with the general sourcing principles of G.S. 105-164.4B.• It defines a retailer as the obligor when the obligor sells the service contract to the purchaser at retail. If the service contract is sold to the purchaser by a facilitator, the facilitator is the retailer unless the facilitator and the obligor have a contractual agreement that the obligor will be liable for payment of the tax. In this instance, the facilitator must send the retailer the tax due on the sales price of or the gross receipts derived from the service contract within 10 days after the end of each calendar month. A facilitator that does not send the retailer the sales tax due is liable for the tax. A facilitator is defined as a person who contracts with an obligor to market the service contract and accept payment for the contract. These provisions are substantially the same as the provisions that apply to a facilitator who accepts payment of sales tax on accommodations.• It moves the exemptions from G.S. 105-164.13 and places them in the newly created statute.• It adds an exemption for items subject to tax under Article 5F, the 1% excise tax on mill machinery and other similar transactions.• It clarifies that the tax does not apply to service contract for items sold at retail that become part of real property unless the service contract is sold at the same time as the item of tangible personal property covered in the contract. The tax does not apply to security or similar monitoring contracts for real property or to a renewal of a service contract where the tangible personal property covered by the contract becomes part of or affixed to real property prior to the effective date of the renewal.• It requires a retailer to report the sales price of or gross receipts derived from a service contract on an accrual basis, so that the receipts are recognized when the transaction occurs rather than when payment is received. Some service contracts are financed over time. This provision clarifies that the sales tax is due at the time of the retail sale and not at the time of the periodic payments.

(d)	<p>Creates a new statute for refunds of sales tax paid on a rescinded sale or a cancelled service. Historically, retailers have provided purchasers a refund of the sales tax paid on tangible personal property that is returned to the retailer for a refund. The retailer is allowed to reduce taxable receipts on the subsequent sales tax return by the taxable amount of the refund for the period in which the refund occurs or may request a refund of an overpayment of tax. This section codifies this current practice.</p> <p>The new statute creates a process to allow a purchaser of a service contract a refund of the sales tax paid. The process is different for a service contract because often the refund is provided by a person who was not the retailer that sold the service contract. This situation becomes more uncertain when the service contract is for a motor vehicle. Under the bill, if the purchaser receives a refund on any portion of the sales price of a service contract purchased from the retailer who collected the sales tax on the retail sale, then the general provisions applicable to rescinded sales apply. If the purchaser receives a refund from anyone else and the amount refunded does not include the sales tax paid on the refundable amount, then the purchaser may apply directly to the Department of Revenue for a refund. An application for a refund must be supported by documentation on the taxable amount of the service contract refunded to the purchaser and it must be filed within 30 days after the refund is received. A sales tax refund filed after the due date is barred.</p>
(e)	<p>Makes a conforming change.</p>
(f)	<p>Clarifies the exemption applicable to an item used to maintain or repair tangible personal property pursuant to a service contract. The exemption does not apply to an item used to maintain or repair mill machinery and other items taxable under Article 5F, since the service contract applicable to this tangible personal property is not subject to tax. The exemption does not apply to a tool, equipment, or similar item of tangible personal property used to complete the maintenance or repair unless the item becomes a component or repair part of the item for which the service contract is sold. For example, the exemption does not apply to the hammer and screwdriver used to do the work under a service contract.</p>
(g)	<p>Clarifies that the gross receipts derived from a service contract for a motor vehicle are not subject to the highway use tax.</p>
(h)	<p>Conforming change to the local sales tax statutes.</p>

EFFECTIVE DATE: This Part of the act would become effective October 1, 2014.

PART VII. RETAILER-CONTRACTORS

SUMMARY: *Part VII of the Omnibus Tax Law Changes bill addresses the applicability of the sales tax laws to retailer-contractors, such as the major home improvement stores, when they are engaged in a performance contract rather than a retail sale. Specifically, a retailer-contractor would be considered the consumer of the items or materials they furnish and install or apply to real property to the extent the item becomes part of the real property. As the consumer of those items, the retailer-contractor would be responsible for payment of the tax rather than the customer. This Part would become effective January 1, 2015.*

CURRENT LAW: Under current law, retailers are required to collect and remit sales tax on retail sales of tangible personal property. Under a performance contract, the contractor agrees to furnish the necessary materials, labor, and expertise to accomplish the job; it is not a contract for the sale of specific items. Contractors are deemed to be the consumers or end users of the tangible personal property they use in fulfilling performance contracts and are liable for the tax. However, when a customer purchases an item from a home improvement store and enters into a contract with the store for the installation of the item in their home, it is not always clear whether that transaction is a retail sale plus installation or a performance contract.

The statutes provide little guidance as to what the correct interpretation is. They do not define "contractor" or "performance contract" or speak to when the installation of tangible personal property constitutes a real property improvement. The definition of "sale" refers to when title or possession is transferred. When a contractor permanently affixes an item of tangible personal property to real estate, title and possession typically transfer upon installation. However, once the item is permanently affixed to real property, general principles of real estate law provide that the item is no longer tangible personal property but has transformed into a real property fixture. Therefore, when a homeowner obtains title or possession to the property, the property is real estate and, therefore, one could argue no retail sale of tangible personal property has occurred. Adding further confusion to the mix, North Carolina's definition of "retailer" includes the business of installing tangible personal property regardless of whether it is permanently affixed to real property. This definition suggests that all contractors are also retailers, which conflicts with other principles at play.

The Department has developed guidance on this issue through its technical bulletins, and the tax treatment is ultimately determined by looking at a number of factors, such as whether an item is sold with an installation agreement, the tenor of the agreement, if there is one, whether an item is pre-fabricated, whether an item is built on-site, and whether a specific quantity is stated in the agreement. Determining the tax consequences involves a complex and fact-specific analysis. Over the years, the guidance has been inconsistent and, at the very least, confusing. For example, the sale and installation of the same item, such as carpet, may have different tax treatment depending on who the seller is and how the transaction is structured. Also, transactions that seem to be similar in nature, such as the installation of countertops and cabinets, are treated differently as well.

For several years, the Department has sought clarification from the General Assembly on this issue. The Revenue Laws Study Committee first studied it in 2012, with no recommendation, and again in 2013 recommending this legislation.

BILL ANALYSIS: Part VII of this act provides that the general rate of tax applies to the sales price of tangible personal property sold to a real property contractor when that property is used by the contractor for the improvement, alteration, or repair of real property and the item becomes part of the real property. The bill defines the term "retailer-contractor" as an entity that can act either as a retailer or as a real property contractor. The sales tax provisions applicable to a real property contractor would apply to a retailer-contractor when it is acting as a real property contractor. Retailer-contractors may continue to make tax-exempt purchases of materials, as they do now, but would accrue and pay the tax once the items are withdrawn from inventory and used in the performance of a real estate improvement contract. If the retailer-contractor uses a subcontractor to perform the installation, then the subcontractor would pay the tax on any items the subcontractor purchases in fulfilling the contract. However, in accordance with existing use tax principles, the retailer-contractor and the subcontractor would be jointly and severally liable for the tax.

The second part of the proposal holds harmless retailers that have been following the law as interpreted by the Department, such as Home Depot, as well as retailers who have asserted that the Department's interpretation is inconsistent with existing statutes, such as Lowe's.

EFFECTIVE DATE: This Part of the act would become effective January 1, 2015, and would apply to sales on or after that date and contracts entered into on or after that date.

BACKGROUND: This issue drew particular attention in 2009 when newspaper reports revealed a long-running dispute between Lowe's and the Department of Revenue on the application of the law in this area. The report indicated that Lowe's was not collecting sales tax when it sold and subsequently installed items such as cabinets, flooring, and countertops. The Department's position is that these transactions are retail sales plus installation and that Lowe's should be collecting sales tax on the purchases but not the installation charges as long as those charges are separately stated on the customer's invoice. Lowe's position is that these transactions are performance contracts and, therefore, they are only required to pay the use tax because they are the user or consumer of that property and that the cost is factored into the "contract price" ultimately paid by the customer, but it is not a separately stated cost.

PART VIII. OTHER SALES TAX CHANGES

SUMMARY: *Part VIII of the Omnibus Tax Law Changes bill makes various sales tax changes.*

CURRENT LAW, BILL ANALYSIS, AND EFFECTIVE DATE:

Section	Explanation	Effective Date
8.1	<p>This section moves the substance of the law imposing the State sales tax on accommodations to a new statutory section for stylistic purposes. The only substantive change provides that a private residence or cottage rented for fewer than 15 days that is listed with a real estate broker or agent is subject to sales tax and occupancy tax. Beginning in 1984, the Department of Revenue interpreted the private residence exemption to apply only if the residence was not listed with a real estate agent. A 1988 memo by an Associate Attorney General supported this interpretation. In 2012, the Department changed its interpretation and issued an Important Notice indicating that the sales tax exemption applied to a private residence rented for fewer than 15 days regardless of whether it was listed with a real estate agent.</p> <p>The current law states that "<i>The tax does not apply to a private residence or cottage that is rented for fewer than 15 days in a calendar year...</i>", but it goes on to state that "<i>A person who, by written contract, agrees to be the rental agent for the provider of an accommodation is considered a retailer under this Article and is liable for the tax.</i>" The Department has requested that language be added to the statute that is consistent with its pre-2012 interpretation.</p> <p>This change would impact the application of occupancy tax as well because G.S. 155A-155 and 160A-215 provide that "<i>the room occupancy tax applies to the same gross receipts as the State sales tax on accommodations and is calculated in the same manner as that tax.</i>"</p>	<p>This section would become effective June 1, 2014, and apply to private residences occupied as a transient accommodation on or after that date even if the accommodation was reserved or paid for prior to the effective date.</p>

8.2	This section disallows a sales tax refund for sales tax paid on video programming and piped natural gas. Historically, the State sales tax refunds allowed to nonprofits and local governments has not applied to sales tax paid on utilities. Prior to 1995, when piped natural gas was subject to sales tax, piped natural gas was included in the list of utilities for which a sales tax refund was not allowed. Last session, when the General Assembly made the policy decision to return piped natural gas to the sales tax base, this conforming change was not considered or made. Likewise, when the General Assembly made the policy decision to begin taxing video programming as a utility, a conforming change to the refund statutes was not considered or made. This section treats utilities that are taxed by the State at the combined general rate the same.	This section becomes effective July 1, 2014, and applies to purchases occurring on or after that date.
8.3	Subsection (a) repeals the sales tax exemption for sales from vending machines of one cent per sale. The provision is obsolete. S.L. 2013-316 removed the sales tax exemption applicable to newspapers sold by street vendors, newspaper carriers, and vending machines. The intent was to tax all newspapers at the State and local sales tax rate. However, G.S. 105-164.13(50) exempts 50% of the sales price of items sold through a coin-operated vending machine from sales tax. To maintain the intent of the 2013 tax law change, subsection (b) provides that the sales tax exemption applicable to 50% of the sales price of items sold through a vending machine does not apply to newspapers. The law currently excludes tobacco products sold through vending machines from this 50% exemption.	This section becomes effective October 1, 2014, and applies to sales made on or after that date
8.4	Effective January 1, 2014, S.L. 2013-316 increased the State sales tax rate on manufactured and modular homes. In response to industry concerns, this section imposes the tax on ½ of the price of the home by exempting 50% of the sales price from sales tax. The industry states that the average material cost in a factory-built home is approximately 50% of the invoice price. The intent of this section is to more closely tax manufactured and modular homes in a similar manner as stick-built homes.	This section becomes effective July 1, 2014.

PART IX. EXCISE TAX CHANGES

SUMMARY: Part IX of the Omnibus Tax Law Changes bill makes various changes to the excise tax statutes, as requested by the Excise Tax Division of the Department of Revenue.

CURRENT LAW, BILL ANALYSIS, AND EFFECTIVE DATE:

Section	Explanation	Effective Date
9.1	Subsection (c) of this section applies to the excise tax on alcohol. It would allow a wholesaler or importer of malt beverages and wine to provide security to the Secretary in the form of a letter of credit as an alternative to a bond. This form of security is consistent with what is currently allowed under	When it becomes law

	the excise tax statutes for motor fuels and tobacco products. This subsection also removes the option of a taxpayer providing security in the form of a bond based upon obligations of a governmental unit. This option has not been used in recent memory and is not a form of collateral allowed in other tax schedules. In the few instances where it has been used, the Department's experience has shown that the bonds are often rolled over into a personal CD when the bond matures rather than another governmental bond. Subsections (a) and (b) of this section modernize the statutes and clarify that the letter of credit must be issued by a bank acceptable to the Secretary and available to the State as a beneficiary.	
9.2	This section would allow a wholesale dealer or retail dealer of other tobacco products to provide the Department a manufacturer's tax affidavit in lieu of a notarized tax affidavit as supporting documentation for a tax refund. A dealer that has stale or unsalable tobacco products upon which the tax has been paid is allowed a refund of that amount. The majority of states allow a dealer to use manufacturer tax affidavits as supporting documentation. The allowance of a written certification from the manufacturer signed under perjury of law does not lessen the accountability of the taxpayer and it expedites the administration of the refund. The change in the statute has been requested by taxpayers. ⁹	When it becomes law
9.3	This section would amend the tax secrecy provisions as follows: <ul style="list-style-type: none"> To allow the Department to furnish a data clearinghouse the information required to be released in accordance with the State's agreement under the December 2012 Term Sheet Settlement, as finalized by the State in the NPM Adjustment Settlement Agreement, concerning annual tobacco product sales by a nonparticipating manufacturer.¹⁰ To allow the Department to share information with a person who provides a surety bond or irrevocable letter of credit on behalf of a taxpayer if the information is necessary for the Department to collect on the bond or letter of credit in the event the taxpayer does not comply with the tax laws. 	When it becomes law
9.4	This section would allow the Secretary of Revenue to delegate the authority to hold hearings. Under administrative practice, this authority has been delegated to a staff attorney.	When it becomes law
9.5	This section clarifies that the tax on motor carriers applies to both intrastate motor carriers and to interstate motor carriers. It also updates the reference to the International Fuel Tax Agreement from June 1, 2010, to July 1, 2013. The update in the reference does not make any substantive changes to the tax laws concerning motor carriers.	When it becomes law
9.6	Section 9.6 clarifies that local sales tax is due on motor fuel for which a	When it

⁹ U.S. Smokeless Tobacco Brands operates a secure website that allows distributors to access affidavits and credit memos for their returns. Each affidavit includes an accurate list of product eligible for return in a state along with an electronically signed statement.

¹⁰ S.L. 2013-360, the Current Operations and Capital Improvements Appropriations Act of 2013, shows \$137,500,000 in adjustments to availability for both FY13-14 and FY14-15 associated with the Tobacco Mast Settlement Agreement.

9.10	refund of the per gallon excise tax is allowed. Under current law, the State sales tax is deducted from any amount of excise tax refunded. This section clarifies that the local sales tax revenue is also deducted from any amount of excise tax refunded. Section 9.10 clarifies the amount of local sales tax to be deducted from a refund of excise tax paid.	becomes law
9.7	This section would tax all biodiesel fuel. B100 is not subject to federal excise tax, and as such is not subject to the State excise tax. B99.9 is subject to the State excise tax since it is a blended product. B100 is most commonly used as a motor fuel.	October 1, 2014
9.8	This section would allow the Secretary to waive or reduce civil penalties imposed under the motor fuel tax statutes under the Department's penalty waiver policy used for other tax schedules. Under current law, a person assessed a civil penalty under the motor fuel tax laws must pay the penalty at the time it is assessed and file a request for a Departmental review of the penalty. Under the change proposed by this section, the penalty would not automatically be payable upon assessment and the administrative process for waiving or reducing it would be simpler and less time consuming. Although a taxpayer must go through the review process for the waiver or reduction of a penalty, the guidelines used to make the decision are the same guidelines currently applied through the penalty waiver policy.	When it becomes law
9.9	This section would clarify that a shipping document required by the vessel transporting motor fuel is intended to provide permanent information. Under current law, if the document is issued by a refiner or a terminal operator, the document must be machine printed. That requirement is not there for a tank wagon importer. A tank wagon importer is a person who imports motor fuel from a terminal or bulk plant in another state and transports the fuel only by means of a tank wagon. A tank wagon is a truck designed to carry at least 1,000 gallons of motor fuel but is not a transport truck. Motor fuel investigators have found shipping documents to be notes contained on a "grease board" or chalk board or other type of device that can be erased.	October 1, 2014
9.10	Removes obsolete references to the privilege tax.	

PART X. TAX LAW COMPLIANCE CHANGES

SUMMARY: *Part X of the Omnibus Tax Law Changes bill would require filing all State tax returns and paying all State taxes to receive and hold an ABC permit. Part X of the bill draft also would authorize the Department of Revenue to use \$500,000 (currently, \$150,000) from the collection assistance fee account to contract for taxpayer locator services.*

CURRENT LAW: G.S. 18B-900 lists the following requirements to receive and hold an ABC permit:

- Be at least 21 years old (19 years old for managers selling only beer and wine).
- Be a NC resident unless the out-of-state person is not responsible for operations.

- Not have been convicted of a felony within 3 years or had citizenship restored.
- Not have been convicted of an alcoholic beverage offense within 2 years.
- Not have been convicted of a misdemeanor controlled substance offense within 2 years.
- Not have had an ABC permit revoked within 3 years except failures to pay registration fee.
- Not have an unsatisfied judgment for injury caused by sales to underage persons.

The requirements under G.S. 18B-900 apply to each of the following persons:

- Owner of a sole proprietorship.
- Managers for a corporation.
- Members of a general partnership.
- General partners in a limited partnership.
- Managers and any members with 25% interest in a limited liability company.
- Each officer, director, and owner of 25% of a corporation.

G.S. 18C-141 prohibits the Director of the North Carolina State Lottery Commission from recommending lottery game retailers to the Commission who are not current in filing all State tax returns and paying all State taxes.

G.S. 105-230 suspends the charter of any corporation or a limited liability company that fails to file any tax return or pay any tax. Any act performed or attempted to be performed during the period of suspension is invalid and of no effect unless the charter is reinstated after filing and paying all taxes.

G.S. 105-243.1 imposes a 20% collection assistance fee on overdue tax debts after 90 days.¹¹ The collection assistance fee is credited to a special account and must be applied to the costs of collecting overdue tax debts.

BILL ANALYSIS: The bill would add a new requirement to G.S. 18B-900 that ABC permit applicants file and pay all State taxes. State taxes must be collectable and finally determined to be due for the tax to block an ABC application. This proposal closely follows the statute¹² requiring lottery retailers to file and pay all State taxes. The ABC Commission and the NC Department of Revenue plan to check the State tax compliance of all new and renewing ABC permits starting May 1, 2015.

Procedurally, the ABC Commission will request the Department of Revenue check the State tax compliance status of persons. If the Department of Revenue reports to the ABC Commission that a person is not in State tax compliance, then the person cannot receive an ABC permit until the Department of Revenue reports to the ABC Commission that the person is in compliance. Taxpayers who enter into an installment payment agreement with the Department of Revenue are considered in compliance as long as the agreement is in force.

The requirement of State tax compliance operates like all ABC permit requirements under G.S. 18B-900 – applying to all persons listed in G.S. 18B-900(c) and applying continually to hold a permit. Four types of ABC permits may still be issued without State tax compliance: special occasion permit under

¹¹ The Department of Revenue may not mail the collection assistance fee notice earlier than 60 days after the tax debt becomes collectible under G.S. 105-241.22. A collection assistance fee is imposed on an overdue tax debt that remains unpaid 30 days or more after the fee notice is mailed to the taxpayer.

¹² G.S. 18C-141.

G.S. 18B-1001(8), limited special occasion permit under G.S. 18B-1001(9), special one-time permit under G.S. 18B-1002, and salesman permit under G.S. 18B-1111.

Subsection (b) of Section 10.1 provides that the Administrative Procedure Act (Chapter 150B) does not apply to the ABC Commission's actions when determining State tax compliance and refusing to issue ABC permits and subsection (c) allows the necessary exchange of confidential taxpayer information between the Department of Revenue and the ABC Commission is authorized.

Lastly, this Part authorizes the Department of Revenue to spend \$500,000 annually on taxpayer locator services. The current authorization is \$150,000. The source of the funds is the collection assistance fee imposed on overdue tax debts. The collection assistance fee provides funds to pay for the costs of collecting overdue tax debts which have included personnel at the Department of Revenue that collect taxes, locator services, and infrastructure projects at the Department of Revenue. When attempting to collect overdue taxes, the Department of Revenue uses locator services through contracts with private data services to identify current addresses for taxpayers.

EFFECTIVE DATE: The tax compliance requirement for ABC permits would become effective May 1, 2015. The increase in the amount of the collection assistance fee that may be used to fund locator services would become effective when it becomes law.

PART XI. PROPERTY TAX CHANGES

SUMMARY: *Part XI of the Omnibus Tax Law Changes bill provides for the central assessment of mobile telecommunications property.*

CURRENT LAW, BILL ANALYSIS, AND EFFECTIVE DATE: Under current law, the property is locally assessed by each county. The valuation of this property has become increasingly complex due largely to the rapidly changing technology in the industry and to the frequent acquisitions and mergers of wireless carriers. Central assessment by the Department would simplify the listing process for the industry and ensure uniformity of assessment among the counties. The change is supported by the mobile telecommunications industry, the Department of Revenue, and local governments.

The central assessment would apply to all of the tangible personal property of a mobile telecommunications company and would also include the cellular towers owned by such companies as well as the cellular towers owned by “tower aggregators.” Real property owned or leased by a mobile telecommunications company or tower aggregator would continue to be assessed locally in each county. This section would become effective for taxable years beginning on and after July 1, 2015.

PART XII. PRIVILEGE LICENSE TAX CHANGES

SUMMARY: *Part XII of the Omnibus Tax Law Changes bill would repeal the existing authority for cities to levy a privilege license tax and would replace it with a new authorization for cities to levy a business tax of up to \$100 on each business location within the city. The new authorization would remove all of the prior restrictions and caps on certain businesses with the exception of certain utilities for which cities receive a share of tax revenue. It also repeals the more limited county authority to levy a privilege license tax. This Part would become effective July 1, 2015.*

CURRENT LAW & BILL ANALYSIS:

Levy and Scope. – Under current law, a city has the authority to levy a privilege tax on all trades, occupations, professions, businesses, and franchises carried on within the city, subject to certain limitations.¹³ These limitations range from outright prohibitions on certain businesses and professions to a cap on the amount of tax for other types of businesses. Otherwise, there is no statutory restriction on the amount of tax that may be charged. It may be in the form of a flat tax or a tax measured by gross receipts. Over 300 cities levy a privilege tax, producing significant revenue for about seven cities: Charlotte, Raleigh, Greensboro, Durham, High Point, Lumberton, and Hickory.

Under this proposal, cities would have the option of levying a business tax of up to \$100 on each business operating within the city. A "business" is broadly defined as a retailer, a wholesale merchant, a service provider, a manufacturer, a franchise, or a nonprofit other than a 501(c)(3). The tax would apply to each business location. "Location" is defined as a uniquely identifiable geographic site or place from which one or more business units wholly or partly operates on a permanent or temporary basis. Accordingly, a business would be subject to the tax for each of its locations within a city, and a single location may house more than one business entity. Under current law, a business need not have a physical location within a city in order to be taxed; the business or trade need only be "carried on" within the city. For example, a landscaping company that has its only office in City A and performs landscaping services in Cities B, C, and D may be taxed by all of those cities. Under this proposal, the company could only be taxed in the city in which it has its physical business location.

This proposal also eliminates the multitude of restrictions and caps on various types of trades, businesses, and professions that exist either by virtue of the repealed Schedule B or existing State privilege license tax statutes. For example, cities are currently prohibited from levying a privilege license tax on certain professionals who are taxed at the State level, such as attorneys, physicians, engineers, real estate brokers, and home inspectors. This proposal removes that restriction but limits the local tax to the business entity that employs the individual or with whom the individual is otherwise affiliated. Other businesses that cities are currently prohibited from taxing include banks, private protective services, burglar alarm dealers, household appliance dealers, and office equipment dealers. These restrictions are removed.

Approximately 64 types of businesses are subject to a cap on the amount of tax that a city may impose. Examples of businesses whose rate is capped at less than \$100 include: amusements, \$25; collection agencies, \$50; peddlers of farm products, \$25; contractors, \$10; restaurants, \$42.50; barbershops & beauty parlors, \$2.50 per person employed; firearms dealers, \$50; auto dealers, \$25.

Prohibition. – Just as under current law, cities would still be prohibited from levying any license, franchise, privilege, or business taxes on the following businesses because cities receive a share of sales tax revenue levied on these businesses:

- Piped natural gas
- Telecommunications
- Video Programming
- Electricity

Administration. – The business tax would be administered the same way that it is now. A city would have to adopt an ordinance setting out the rate schedule. The tax would be levied on an annual basis and

¹³ G.S. 160A-211(a), the subsection that authorizes cities to levy a privilege license tax, was inadvertently repealed in Section 58(b) of S.L. 2013-414. The repeal was a drafting error as evidenced by the fact that Section 58(d) of that same act amends the same subsection and leaves the remainder of the statute intact. Section 12.1 of this proposal reenacts the provision to correct the error.

would be due by July 1 of each year. The penalties and collection remedies would essentially be the same as they are now.

Counties. – Section 2 of the bill repeals a county's authority to levy a privilege license tax. Based on the most recent data available, only 37 counties levy a privilege license tax and generate a cumulative total of less than \$500,000.

EFFECTIVE DATE: This Part would become effective July 1, 2015.

PART XIII. LICENSE PLATE AGENT COMPENSATION

SUMMARY: *Part XIII of the Omnibus Tax Law Changes bill sets the LPA transaction rate for the collection of property tax under the Tax & Tag Together program at the transitional rate of \$1.06, clarifies the increased rate applies to all transactions where an LPA collects property tax as of July 1, 2014, and allows the retroactive portion of the fee increase to be paid out over a three month time period.*

CURRENT LAW: The Division of Motor Vehicles (DMV) is required to ensure, as far as practicable and possible, that registration and registration renewals for motor vehicles may be issued through license plate agents (LPAs) located in every community across the State. DMV enters into commission contracts with individuals to perform this service. The local tag agents are compensated on a per transaction basis. The standard rate for a transaction is \$1.43. Unless otherwise provided, the performance of one or more transactions at the same time is considered a single transaction for purposes of compensation. Certain transactions are always considered separate transactions and allowed a different rate of compensation. The collection the highway use tax is considered a separate transaction and compensated at \$1.27.

In September 2013, the State began implantation of a combined system for motor vehicle registration renewal and property tax collection. Under the new Tax & Tag Together program, the motor vehicle owner will receive one bill, and make one payment for both property taxes and vehicle registration renewal. The Tax & Tag Together program also provides for the issuance of a temporary registration plate if property taxes are not paid with the issuance of a new plate. A person may be issued a limited registration "T" sticker for the temporary registration plate.

S.L. 2013-372 provided increased compensation for LPAs new duties required under the Tax & Tag Together program. The collection of property taxes and the issuance of a "T" sticker" are recognized as separate transactions for the purpose of compensation. The transaction rate for the issuance of a "T" sticker was set at \$1.27, effective July 1, 2013. The transaction rate for collecting property tax with registration renewals for the transitional period of the first six months of the Tax & Tag Together program was set at \$1.06. The transaction rate after the first six months for both new registration and renewals was set at \$0.71.

BILL ANALYSIS: Part XIII sets the LPA transaction rate for the collection of property tax under the Tax & Tag Together program at the transitional rate of \$1.06. The transitional rate will apply to the collection of property taxes with registration renewals for the entire 2013 fiscal year. The draft also clarifies the increased rate applies to all transactions where an LPA collects property tax, effective July 1, 2014, therefore, setting the transitional rate of \$1.06 per transaction to all collections of property tax by LPAs for the 2014 fiscal year and thereafter.

Below is a chart that shows the recent changes in the compensation to LPAs, as well as the proposed increase:

	Transaction fee to LPAs for collection of:				
	Property tax with renewal		Property tax with new registration		Property tax with new registration and renewals
	July 2013 – March 2014	March 2014 – July 2014	July 2013 – March 2014	March 2014 – July 2014	July 2014 and thereafter
Prior to 2013-372	\$0.48	\$0.48	\$0.48	\$0.48	\$0.48
2013-372	\$1.06	\$0.71	\$0.71	\$0.71	\$0.71
Draft proposal	No change	\$1.06	No change	No change	\$1.06

Under current law, the fee for property tax collection by LPAs for renewals that expire on or after March 1, 2014, will decrease to \$0.71. The draft extends the transitional rate of \$1.06 for the collection of property tax with registration renewals that expire on or after June 30, 2014. If enacted, the draft proposal would direct DMV to calculate the difference in the payments made under the current law and the proposed increase in this draft by September 1, 2014. The difference in the two rates would be paid to LPAs by deducting the appropriate amount of the property tax revenues remitted to the counties. The payment to the LPAs and the corresponding reduction in the payments to the counties would be made in equal amounts over a three month period.

The bill also clarifies the increased fee for property tax collection applies to all transactions where a LPA collects property taxes, effective July 1, 2014.

DMV receives compensation from the counties for the duties it performs under the Tax & Tag Together program. A conforming change made in S.L. 2013-372 has been interpreted to provide DMV with an increase in the fee it receives for the collection of property tax to mirror the amount paid to LPAs. This draft maintains the increase in the fee to \$0.71 for DMV provided in S.L. 2013-372, but does not provide DMV with the increase provided LPAs in this draft. The fee provided to DMV will be the amount set in the Memorandum of Understanding (MOU) signed by the Department of Revenue and the Division of Motor Vehicles. Future MOUs can amend the transaction fee paid to DMV, but the fee cannot exceed the per transaction fee allowed for LPAs.

EFFECTIVE DATE: The portion of this Part related to the fee for registration renewals would become effective March 1, 2014. The remainder of this Part would become effective July 1, 2014.

PART XIV. TECHNICAL, CLARIFYING, & ADMINISTRATIVE CHANGES

SUMMARY: *Part XIV of the Omnibus Tax Law Changes bill makes clarifying, conforming, and administrative changes to the various tax laws. Unless otherwise stated, this Part would become effective when it becomes law.*

CURRENT LAW, BILL ANALYSIS, AND EFFECTIVE DATE:

Section	Explanation and Effective Date
14.1	This section corrects a cross reference.
14.2	<p>This section replaces two outdated references with respect to qualifying for the major recycling facility tax credits. First, it replaces the term "enterprise tier one area" with the term "development tier one area." The current statute requires that, at the time the owner begins construction, the facility be located in an enterprise tier one area. The term "enterprise tier one area" was part of the Bill Lee tax credits, which expired in 2007. The current equivalent term, originating with the enactment of the Article 3J tax credits, is "development tier one area." A development tier one area is a county whose annual ranking is one of the 40 highest in the State.</p> <p>Second, it deletes the wage standard requirement to be consistent with the current law as it applies to a tier one area. In 2002, the General Assembly eliminated the wage standard for enterprise tier one and two areas¹⁴ but a conforming change was not made to this statute. At the time, there was only one taxpayer that qualified for the credit, and the wage standard was only required to be met at the time construction began on the facility, which had already occurred. However, to the extent there may be taxpayers who qualify for this credit, which is only available in a tier one area, in the future, the statute should be amended to reflect the fact that the wage standard is no longer a requirement in a tier one area.</p>
14.3	This section inserts a word that was inadvertently omitted.
14.4(a)	This section deletes the definition of "Dependent" because the term is not required after the changes made by House Bill 998, S.L. 2013-316.
14.4(b) &14.5	This section updates the terminology used in the statutes authorizing withholding of income tax from wages. After House Bill 998, S.L. 2013-316, "exemptions" are not part of the computation of estimated tax to withhold from wages. Instead, the Department of Revenue uses the term "allowances."
14.6	This section deletes a statutory formula used to calculate the amount of estimated tax to withhold from pension payments where the recipient fails to file a withholding tax form. After House Bill 998, S.L. 2013-316, the statutory formula no longer approximates recipient's tax liability. Recipients who do not complete the tax form to calculate withholding from pension payments will be treated the same as employees who do not complete the tax form.
14.7	This section makes technical changes to sales tax definitions. It deletes the word "retail" within the definition of "net taxable sales" because the term is already included by virtue of the definition of the term "gross sales." It also deletes the word "the" in the definition

¹⁴ S.L. 2002-172.

	of "retailer" because "engaged in business" is the proper defined term.
14.8	This section makes various technical changes to the sales tax imposition statute.
14.9	This section clarifies that a facilitator who is liable for tax ¹⁵ must obtain a certificate of registration like other retailers. A facilitator is a person, other than a real estate agent, who contracts with a provider of an accommodation to market the accommodation and who accepts payment from the consumer for the accommodation. An example of a facilitator would be an online travel company like Expedia, Orbitz, or Priceline.
14.10	<p>This section provides for the applicable due date for a sales tax payment if the due date falls on a weekend or holiday or on a day that the Federal Reserve Bank is closed, which prohibits a person from making a payment by ACH¹⁶ Debit or Credit.</p> <p>These provisions are currently contained in an informational document on the Department's website, but there is not a specific statute, other than one that applies only to payment of property taxes.¹⁷</p>
14.11	This section changes from March 1 to March 15 the annual due date for the captive insurance tax return. S.L. 2013-116 provided that the annual report due date for some captive insurance companies is March 1 and, for others, such as a pure captive, it is March 15. The tax returns for all captives are due March 1. This year, the pure captive insurance companies filed premium tax returns by the March 1 due date and attached to the return copies of pages from their annual reports in support of the premium information marked "draft" since the tax return was due before the financial statement. This issue would be eliminated by changing the due date for all premium tax returns to March 15.
14.12	This section makes one technical change and one substantive change. The technical change corrects a statutory reference. The substantive change would add a new criminal offense to the list of offenses for which the Secretary of Revenue may appoint employees of the Criminal Investigations Division to serve as revenue law enforcement officers. The new offense, which was created by the General Assembly in 2013, is for the possession, transfer, or use of an automated sales suppression device, informally known as "tax zipper software."
14.13	<p>This section provides the Department of Revenue with guidance on how to treat amended returns filed under two repealed taxes. Subsections (a) and (b) provide guidance for amended returns filed under the franchise tax on electricity. Subsections (c) and (d) provide guidance for amended returns filed under the excise tax on piped natural gas. Subsections (e) and (f) clarify that only cities that received a distribution under the repealed franchise tax and excise tax will receive distributions from the new sales tax on electricity and piped natural gas.</p> <p>The Tax Reduction Act, S.L.2013-316, included electricity and piped natural gas in the State sales tax base while repealing the utility franchise tax on electricity and the excise</p>

¹⁵ Under G.S. 105-164.4(a)(3), a facilitator must send the retailer the portion of the sales price that the facilitator owes the retailer plus the tax due once the accommodation rental marketed by the facilitator is completed. A facilitator that does not send the retailer the tax due on the sales price is liable for the amount of tax the facilitator failed to send.

¹⁶ Automated Clearing House Debit is a method of payment that enables companies to electronically withdraw funds from bank accounts using bank routing numbers and individual account number.

¹⁷ G.S. 105-395.1.

	<p>tax on piped natural gas. A portion of both of the repealed taxes was shared with the cities. The Tax Reduction Act replaced the tax-sharing revenue under the repealed taxes with a distribution of part of the sales tax on electricity and piped natural gas. The amount distributed to each city under the sales tax is based on the distribution under the repealed taxes the last year those taxes were in effect.</p> <p>Utilities are allowed to file amended returns on the repealed taxes for up to three years. Amended returns filed on the repealed taxes can change both distributions under the repealed taxes and the amount to be distributed to cities under the new sales tax on electricity and piped natural gas. These sections provide guidance to the Department on how to treat amended returns that change past and future distributions. First, it provides that any additional funds needed for increases to past distributions under the repealed taxes can be drawn from the sales tax revenue. Second, it creates a date certain for the future distributions to be determined. The Department of Revenue will set the distributions for each fiscal year by September 15 using amended returns processed by the Department prior to July 31 of that year.</p>
14.14	<p>Property that is appraised at its present use value may remain in the program if the property is under an enforceable conservation easement that would qualify for the conservation easement tax credit. S.L. 2013-316 repealed the conservation easement tax credit for taxable years beginning on or after January 1, 2014. The repeal of the tax credit was not intended to effect property in the present use value program. This section puts the applicable provisions that were provided in the tax credit statutes in Chapter 113A and makes the necessary conforming changes in other statutes.</p>
14.15	<p>This section deletes an inconsistent effective date for the repeal of G.S. 105-159.2 which formerly allowed a taxpayer to checkoff a donation to the North Carolina Public Campaign Fund. Section 38.1.(f) of S.L. 2013-381 repealed G.S. 105-159.2 effective July 1, 2013. This section makes the effective date of a duplicative repeal in Section 21.1.(c) of S.L. 2013 360 effective at the same time.</p>
14.16	<p>This section updates from January 2, 2013, to December 31, 2013, the reference to the Internal Revenue Code. This change keeps the statute up to date, but does not result in any substantive changes because there have not been any federal tax law changes since January 2, 2013, that impact the calculation of North Carolina taxable income.</p>
14.17	<p>This section changes the name of the document filed by the Secretary of Revenue to release an erroneous tax lien. Currently, the Department of Revenue files a “certificate of release” that credit reporting agencies treat as a negative item on a credit report. The renamed document, “certificate of withdrawal,” is expected to cancel the original tax lien without impacting the taxpayer’s credit report. This section is effective when it becomes law.</p>
14.18	<p>S.L. 2013-157 made a number of changes to North Carolina's Limited Liability Company Act. Among the changes was a new defined term of "company official" defined as: "<i>Any person exercising any management authority over the limited liability company whether the person is a manager or referred to as a manager, director, or officer or given any other title.</i>" This section incorporates the new term into the responsible person statute, which provides for personal liability when certain taxes are not paid.</p> <p>The section also removes the limitation on the type of withholding taxes that can be collected from a responsible person. Current law allows the Department of Revenue to hold business operators liable for income tax withheld on employee wages. This section</p>

	eliminates the requirement that the withholding be for employee wages. For example, withholding on independent contractors could now be collected from responsible persons. This section is effective when it becomes law.
14.19	This section updates a statutory reference.
14.20	S.L. 2013-316 repealed the individual income tax credit for property taxes paid on farm machinery. This section removes references to the tax credit that are no longer needed in the property tax statutes.
14.21	This section makes a technical correction by adding (32a) to the list of exempt inventories for which a person need not provide a report under G.S. 105-315 and makes stylistic changes to update the statute.
14.22	This section repeals an obsolete subsection. G.S. 105-537(d) provides that a county may not levy the one-quarter cent sales and use tax under Article 46 if it also levies the land transfer tax under Article 60. Article 60 was repealed by S.L. 2011-18.
14.23	This section corrects a Session Law reference in last year's Revenue Laws Technical changes act with respect to a local occupancy tax act.
14.24	<p>This section creates a new limited registration plate for vehicles that are registered after the prior registration on the vehicle has expired. Current law provides for a limited registration plate for an initial registration, but there is not a similar provision for registration renewals. This section is designed to solve two customer service problems, one involving military service members, and the second involving appeals for vehicle valuations where the customer has not been given an opportunity to appeal the valuation.</p> <p>There are instances where an individual can choose not to renew the registration on a vehicle for a year or longer. As long as the vehicle is not being driven, this is allowed under the law. When the vehicle will be operated again, the owner must renew the vehicle registration. Under Tax & Tag Together, when the individual renews the registration, property taxes on the vehicle for the upcoming tax year are due at the time of renewal.</p> <p>Military service members – The federal Service Members Civil Relief Act provides that personal property (including vehicles) of service members is not subject to personal property taxes simply due to the fact that the member is serving in the state.</p> <p>Active duty service members often do not renew vehicle registrations when the member is deployed overseas. Under Tax & Tag Together, when a service member returns from deployment and seeks to renew a vehicle registration, the system will not allow the vehicle to be registered without payment of the property tax, even if the service member does not owe the tax.</p> <p>Valuation appeals – Under current law, individuals may appeal the valuation assigned to a motor vehicle for property tax purposes. Taxpayers are given notice of the valuation of the vehicle and the right to appeal on the combined property tax notice. The combined notice is sent 60 days prior when the taxes are due. However, if an individual has allowed the registration to lapse more than a year, the individual would not have received a bill and would not have received notice of the tax value for the upcoming property tax year. Under the current system, the taxpayer will not be able to renew the vehicle registration without paying the tax for which the taxpayer did not have the opportunity to appeal.</p> <p>This section allows a temporary limited registration plate to be issued in both of these</p>

	circumstances. Once the limited registration plate is issued, the taxpayer would have 60 days to remedy the tax issue. Once the tax issue has been resolved, the taxpayer could apply for a permanent tag.
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PART XV. TAX VAPOR PRODUCTS/PROHIBIT IN JAILS

SUMMARY: *Part XV of the Omnibus Tax Law Changes bill would provide an excise tax of 5¢ per milliliter to be imposed on vapor products, would prohibit the use of vapor products in State correctional facilities, and would make it a criminal offense to for a person to provide a vapor product to an inmate of a local confinement facility and for an inmate to possess a vapor product.*

CURRENT LAW: Under G.S. 105-113.5, cigarettes are taxed at 45¢ per pack. Other tobacco products (OTP), including pipe tobacco and roll-your-own tobacco is taxed under G.S. 105-113.35 at 12.8% of the cost of the product. The tax on cigarettes is paid by the distributor of the product. The tax on OTP products is payable by the wholesale dealer or retail dealer who first acquires or otherwise handles the product.

A vapor product, commonly known as an electronic cigarette, is a handheld device that produces vapor from a liquid. The liquid is generally heated to produce the vapor by a battery operated device. The liquid usually contains nicotine and sometimes contains flavors. The amount of the nicotine in the liquid can vary. Most electronic cigarettes are reusable. The liquid in the device can either be replenished replacing the cartridge that holds the liquid, or by manually refilling the liquid container.

In 2009, Congress enacted the Family Smoking Prevention and Tobacco Control Act, which gave the US Food and Drug Administration (FDA) the authority to regulate new tobacco products including e-cigarettes, nicotine gels, cigars, pipe tobacco, and dissolvable nicotine products.

In April 2014, the FDA issued proposed rules to regulate e-cigarettes. The proposed rules will be subject to 75 days of public comment. The proposed rules deem e-cigarettes a "tobacco product" for the purpose of federal regulation. The rules further propose to subject e-cigarettes to the following restrictions:

- Enforcement against adulterated or misbranded products.
- Ingredient disclosure and reporting of harmful components
- No modified risk descriptors (light cigarettes)
- No free samples
- Premarket review
- Minimum age for purchase

G.S. 148-23.1 prohibits the use and possession of tobacco products anywhere on the premises of a State correctional facility. Exemptions are provided for use and possession for religious purposes consistent with the policies of the Department of Public Safety (DPS), and also for possession by employees or visitors within the confines of a motor vehicle located in a parking area if the tobacco product remains in the vehicle and the vehicle is locked when the employee or visitor exits the vehicle.

G.S. 14-258.1 provides that it is a Class 1 misdemeanor to do either of the following:

- To knowingly give or sell tobacco products to an inmate on the premises of a correctional facility or in the custody of a local confinement facility, or to a person for delivery to an inmate.

- For an inmate in the custody of a local confinement facility to possess tobacco products.

BILL ANALYSIS: This Part of the bill does two things:

Excise tax: Section 15.1 of Part XV would impose an excise tax of 5¢ per milliliter of the consumable product of vapor products. Vapor products are defined as noncombustible products that use a heating element to produce vapor from nicotine in a solution. The consumable product is the part of the vapor product that contains the nicotine liquid solution. All invoices for vapor products must contain the amount of the consumable product in milliliters.

The tax would be administered in a similar fashion to the tax on OTP. The tax will be paid the wholesale dealer or retail dealer who first acquires or otherwise handles the product. The tax does not apply to products sold outside the State, products sold to the federal government, or products distributed without charge. Taxes are paid monthly. Each dealer must keep sufficient records of vapor products transactions.

Wholesale dealers and retail dealers must obtain a license for each place of business that handles vapor products. The license fee for wholesale dealers is \$25, and the license fee for retail dealers is \$10.

Taxpayers that timely file returns and payments of the taxes on OTP are allowed a discount of 2% of the amount due. This discount will not apply to the tax on vapor products.

No vapor in prisons and jails: Section 15.2(a) of Part XV prohibits the use of vapor products in State correctional facilities. Exemptions are provided for use and possession for religious purposes consistent with the policies of DPS, and for possession by employees or visitors within the confines of a motor vehicle located in a parking area if the vapor product remains in the vehicle and the vehicle is locked when the employee or visitor exits the vehicle.

Section 15.2(b) it a Class 1 misdemeanor for either of the following:

- To knowingly give or sell vapor products to an inmate on the premises of a correctional facility or in the custody of a local confinement facility, or to a person for delivery to an inmate.
- For an inmate in the custody of a local confinement facility to possess vapor products.

EFFECTIVE DATE: The provisions related to imposing the excise tax on vapor products would become effective February 1, 2015. The provisions related to vapor products in State and local confinement facilities would become effective December 1, 2014.

PART XVI. CHANGE CORPORATE APPORTIONMENT FORMULA TO FOUR TIMES THE SALES FACTOR

SUMMARY: *Part XVI of the Omnibus Tax Law Changes bill amends the apportionment formula for the calculation of corporate income and franchise tax.*

CURRENT LAW: In order to tax multistate corporations, states must determine the amount of the corporation's business that is attributable to that state for tax purposes. States make this determination by calculating an apportionment percentage. Multistate corporations multiply their income and franchise tax base by this apportionment percentage to calculate their corporate tax liability.

States generally look at three factors to calculate the apportionment percentage:

- The percentage of the corporation's property located in the state.
- The percentage of the corporation's payroll located in the state.

- The percentage of the corporation's sales in the state.

The states vary in how they assign weight to these three factors. An equally weighted apportionment formula would provide that each of the three factors are weighed equally. For most corporations, North Carolina currently uses the property, payroll, and sales factor with a double weighted sales factor.¹⁸ North Carolina currently uses single sales factor apportionment for excluded corporations¹⁹, public utilities, and capital intensive corporations²⁰.

BILL ANALYSIS: Part XVI of the act amends the apportionment formula for the calculation of corporate income and franchise tax by moving from a double weighted sales factor to a four-time weighted sales factor. The change to the apportionment formula does not change the tax liability of the majority of North Carolina companies because their sales are entirely within the State. Of our neighboring states, South Carolina and Georgia use single sales factor apportionment and Virginia uses double-weighted sales with an option to use single sales factor apportionment for manufacturing and retail companies.

EFFECTIVE DATE: This Part of the act would become effective for tax years beginning on or after January 1, 2015.

BACKGROUND: Many believe single sales factor apportionment encourages investment and job creation by rewarding companies that increase their share of property and payroll in the State, and by exporting the tax burden to out-of-state companies that use the state as a market rather than as a location for their jobs, investment, and production activity. Others believe single sales factor apportionment arbitrarily picks winners and losers. For multistate companies whose North Carolina share of company sales is more than their North Carolina share of company property and payroll, single sales factor apportionment will increase their North Carolina income and franchise tax liability.

PART XVII. EFFECTIVE DATE

Except as otherwise provided, this act would become effective when it becomes law.

¹⁸ NC began using a double-weighted sales factor in 1989 as an economic incentive to attract a Nabisco plant to the State. The plant did not locate in the State.

¹⁹ Building contractors, securities deal, loan company, corporation receiving more than 50% of ordinary income from intangible property.

²⁰ A company with \$1 billion in investment.